

April 3, 2006

Mary Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke St
Alexandria, VA 22314-3428

Dear Ms. Rupp:

On behalf of the Association of Credit Union Internal Auditors (ACUIA) Board of Directors and its 600+ members nationwide, the following comments are being submitted in response to NCUA's request for comment of Advanced Notice of Proposed Rulemaking 7535-01-U, Supervisory Committee Audits, regarding whether and how to modify the Supervisory Committee audit rules to obtain an "attestation on internal controls" in connection with the annual audits; to identify and impose assessment and attestation standards for such engagements; to impose minimum qualifications for Supervisory Committee members; and to identify and impose a standard for the independence required of state-licensed compensated auditors.

In November 2004, ACUIA provided comments and recommendations in response to NCUA's Letter to Federal Credit Unions (03-FCU-07), which offered guidance to federal credit unions on selected provisions of the Sarbanes-Oxley Act of 2002 (SOX). Within that response, ACUIA stated that we believe the relevant provisions of SOX are good business practices for credit unions and with development of more specific guidance from NCUA which encompasses the ACUIA recommendations offered, stronger internal control environments within credit unions would result.

Specifically, we recommended NCUA strongly encourage credit unions with assets of \$500 million or more to obtain an opinion audit by a "registered public accounting firm" as defined under SOX and that the supervisory/audit committee have full responsibility over such an engagement. At the time ACUIA also agreed with NCUA's comment to Section 302 of SOX that senior management "should attest to the accuracy, in all material respects, of the financial statements including call reporting." We also suggested that management of all credit unions deciding to supplement their financial statement audit with a Report on Examination of Internal Controls over Call Reporting look to their internal audit function to perform this examination. Lastly, we stated our belief that adequate financial knowledge must exist on the supervisory/audit committee. However, any such financial "expertise" need not be a requirement of all committee members.

In its guidance provided addressing Sections 404 and 407 of the Act specifically, NCUA indicated a credit union may choose to supplement a financial statement audit with a Report on Examination of Internal Controls over Call Reporting. In addition it left open the option of disclosing to NCUA whether or not it has a financial expert on its supervisory committee. There would not appear to be any changes within the environment which would support a change in this view point.

Given the current environment in which the credit union industry is dealing with increasing numbers of banker attacks and lawsuits on credit unions, federal-to-state chartered credit union conversions, credit union to mutual bank conversions, and credit union mergers simply in the realm of survival, the cost and productivity impact of implementing a change at this time may prove over burdensome for credit unions. Further analysis regarding the cost/benefit and how credit unions of varying asset size would be impacted is necessary to ensure any change would apply to the many versus the few.

When evaluating a possible regulatory change, caution must be taken when attempting to compare organizational structure, business sectors, auditing standards, and regulatory environments. Credit unions are member-owned, not-for-profit cooperative financial institutions formed to permit those in the field of membership specified in the charter to save, borrow, and obtain related financial services. As the main purpose behind SOX was to re-establish stock holder confidence in the public sector in light of a few major accounting scandals, enacting similar regulatory requirements on credit unions as those imposed by the SEC or FDICIA on public, profit-oriented organizations would not appear necessary. In addition, the idea of enhancing member service in credit unions as compared to maximizing stock holder confidence, value, and share price would appear to make the need for additional management reporting of the control environment and enhancement of the financial expertise of the supervisory committee less relevant within our industry. As not-for-profit organizations and given the high implementation costs and difficulties reported in several surveys since the introduction of SOX, it would appear that at least for the short term credit unions may not be able to provide the same level of member benefits as they do today if such standards were required.

With these thoughts in mind, the following responses are being provided by ACUIA to the questions submitted by NCUA. It should be noted that they represent the views of ACUIA members and the Board only. They may not represent the views of management at individual credit unions where ACUIA members are employed.

1. Should part 715 require, in addition to a financial statement audit, an "attestation on internal controls" over financial reporting above a certain minimum asset threshold?
No. Traditionally credit unions have believed in the need to maintain an adequate internal control environment and as such larger credit unions have employed internal auditors. NCUA has never opined on whether credit unions should implement an internal audit department once a certain asset size is reached. ACUIA believes that having an internal audit department which reports to the supervisory committee is organizationally beneficial and should be sufficient to ensure the necessary controls over financial reporting exist.
2. What minimum asset size threshold would be appropriate for requiring, in addition to a financial statement audit, an "attestation on internal controls" over financial reporting? **Given the FDIC's recent decision to increase the minimum asset to \$1 billion based on the GAO 2005 recommendation (GAO-06-220T) that credit unions be subject to the same FDICIA requirement it would seem appropriate that if a threshold be established it not be less than \$1 billion. Based on NCUA's 2004 Yearend Statistics for Federally-Insured Credit Unions Report, only 98 of the 5,572, or 1.76% of federally insured credit unions exceed \$1 billion in assets. Therefore ACUIA believes that the cost/benefit to the credit union industry of implementing an additional reporting requirement which**

would impact only a very limited number of credit unions would appear unreasonable.

3. Should this threshold be the same for natural person credit unions and corporate credit unions? **ACUIA believes that as they are both member based, not-for-profit organizations there would not be reason for use of a different threshold.**
4. Should management's assessments of the effectiveness of internal controls and the attestation by its internal auditors cover all financial reporting or should it be more narrowly framed to cover only certain types of financial reporting? **In its response to Section 302 of SOX, NCUA stated that senior management "should attest to the accuracy, in all material respects, of the financial statements including call reporting." ACUIA concurs with this position and as such should only apply to annual financial statement audits and NCUA 5300 call reporting.**
5. Should the same auditor be permitted to perform both the financial statement audit and the "attestation on internal controls" over financial reporting? **Yes. The additional cost of engaging a separate auditor to perform just the attestation would place additional financial burden on credit unions. With that said, ACUIA believes that an internal audit function may be best situated to perform the attestation of internal controls over financial reporting and minimize the additional audit costs. However unless encouraged, supported, and accepted by NCUA, the work perform may still require additional testing by the external auditor to obtain reasonable assurance themselves. This would result in higher audit fees assessed to the credit union.**
6. If the "attestation on internal controls" were required, should it be required annually or less frequently? **ACUIA believes that given the existing control structure, abundance of regulations, quarterly reporting requirements, frequency of examination, a time frame of every three to five years would seem appropriate. Any lesser timeframe would be perceived as placing unnecessary financial and human resource burden on credit unions.**
7. If the "attestation on internal controls" were required, when should the requirement become effective? **ACUIA believes that given the various delays, complications, and high costs seen in the implementation of this requirement within in the public sector, an effective date cannot be determined until more specific requirements and regulatory guidelines are finalized. Existing implementation guidelines are discussed using a two-year timeline, therefore ACUIA believes anything less than 3 years from the requirement finalization date would seem inappropriate.**
8. If credit unions were required to obtain an "attestation on internal controls", should part 715 require that those attestations adhere to PCAOB's AS 2 that applies to public companies, or to the AICPA's revised AT 501 standard that applies to non-public companies? **Most external audit firms follow AICPA audit standards when performing annual financial statement audits for credit unions. It is ACUIA's opinion that as credit unions are not "public" companies, they should not be expected to adopt or adhere to certain SEC rules.**
9. Should NCUA mandate COSO's Internal Control – Integrated Framework as the standard that must be followed or should each credit union have the option to choose

its own standard? **The COSO framework developed by the Treadway Commission is the most widely recognized standard. However, ACUIA believes that all credit unions should have the option to adopt whichever standard is best suited for them and agreeable by their regulator and external auditors, especially since they would be providing attestation to such.**

10. Should supervisory committee members of credit unions above a certain minimum asset size threshold be required to have a minimum level of experience or expertise in credit unions, banking or other financial matters? If so, what criteria should they be required to meet and what should the minimum asset size threshold be? **Like that of board members, supervisory committee members at all credit unions should be representative of its membership. Keeping in mind that credit union committee members are volunteers (non-compensated), credit unions should not be required to solicit individuals solely to meet minimum experience and expertise in financial matters requirements. ACUIA believes that having committee members with varying backgrounds and work experience, not only financial related, may make for an overall stronger and effective committee. As credit union size and complexity increase, so should the level of volunteer knowledge and experience. ACUIA continues to its agreement with NCUA that at least one member of the committee should have “adequate” financial knowledge as defined in Section 407 of SOX. We would suggest that such requirements be further outlined and adopted under the credit union’s bylaws, supervisory committee charter, etc., and not specifically outlined as a requirement by regulation simply based on asset size.**
11. Should supervisory committee members above a certain minimum asset size threshold be required to have access to their own outside counsel? If so, what minimum asset size threshold? **In our opinion, incidental powers granted to the supervisory committee by the board of directors of all credit unions should include the ability to retain outside counsel, as needed, to assist in fulfilling their duties. Such outside counsel does not need to be separate and apart from that which is otherwise retained by the credit union unless a conflict of interest would result. ACUIA suggests that access to outside counsel should be afforded to supervisory committees regardless of asset size.**
12. Should supervisory committee members above a certain minimum asset size threshold be prohibited from being associated with any large customer of credit unions other than the sponsor? If so, what minimum asset size threshold? **ACUIA believes that as supervisory committee members are appointed by the board chair, this should fall under the related due diligence/selection process of the chair, or perhaps nomination committee if one is used by the credit union, in ensuring that no conflict of interest would result if such an individual is appointed. As such, asset size would be irrelevant.**
13. If any of the qualifications addressed in questions 10, 11, and 12 were required of supervisory committee members, would credit unions have difficulty in recruiting and retaining competent individuals to serve in sufficient numbers? If so, describe the obstacles associated with each qualification? **It is ACUIA’s opinion that it may be more difficult for smaller, single SEG or common bond credit unions as the pool of volunteers of which to select from could be limited. What must be considered is if financial knowledge qualifications were to become required,**

what impact would result and would a committee member not meeting financial knowledge qualifications need to step down and be replaced?

14. Should a state-licensed, compensated auditor who performs a financial statement audit and/or “internal control attestation” be required to meet just the AICPA’s independence standards, or should they be required to also meet SEC’s independence requirements and interpretations? If not both, why not? **As mentioned in #8, SEC standards apply to public companies and should not apply to credit unions. In is ACUIA’s position that AICPA standards only would be appropriate.**
15. Is there value in retaining the “balance sheet audit” in existing part 715.7 as an audit option for credit unions with less than \$500 million in assets? **No, there are numerous external audit firms which focus on providing audit services almost exclusively to credit unions. Therefore, the cost of a full financial statement audit is affordable to the majority of credit unions regardless of asset size. ACUIA would suggest that statistical information be obtained to determine current usage by credit unions of a “balance sheet audit.” Should the number be insignificant, this option should be eliminated.**
16. Is there value in retaining the “Supervisory Guide audit” in existing part 715.7 as an audit option for credit unions with less than \$500 million in assets? **This may be applicable only to relatively small credit unions. ACUIA would suggest the threshold for this option not exceed \$100 million in assets. Current numbers of credit unions performing this type of audit would need to be evaluated prior to determining option retention or elimination.**
17. Should part 715 require credit unions that obtain a financial statement audit and/or an “attestation on internal controls” to forward a copy of the auditor’s report to NCUA? If so, how soon after the credit union receives it? **No, as stated in part 715.10 “the Supervisory Committee must verify that the audit was performed and reported in accordance with the terms of the engagement letter prescribed herein. The Supervisory Committee must submit the report(s) to the board of directors, and provide a summary of the results of the audit to the members of the credit union orally or in writing at the next annual meeting of the credit union. If a member so requests, the Supervisory Committee shall provide the member access to the full audit report. If the National Credit Union Administration (“NCUA”) so requests, the Supervisory Committee shall provide NCUA a copy of each of the audit reports it receives or produces.” It is ACUIA’s position that there does not appear to be any precedent which would support a change in the above described process.**
18. Should part 715 require credit union to provide NCUA with a copy of any management letter, qualification, or other report issued by its external auditors? If so, how soon after the credit union receives it? **No. ACUIA believes the review of such information should be included in the work performed during NCUA’s normal examination process and the requirement to submit copies of such information directly to NCUA would simply create unnecessary paperwork and increased regulatory burden.**
19. If credit unions were required to forward external auditor’s reports to NCUA, should part 715 require the auditor to review those reports with the supervisory committee

before forwarding? **As oversight of the annual audit engagement is a primary responsibility of the supervisory committee, ACUIA supports the position that all reports and results should be discussed and reviewed with them and the internal auditor in advance of the forwarding to NCUA.**

20. Existing part 715 requires a credit union's engagement letter to prescribe a target date of 120 days after the audit period-end for delivery of the audit report. Should this period be extended or shortened? What sanctions should be imposed for violations? **ACUIA believes the current target date of 120 days is appropriate. Sanctions, if any, should be on a case by case basis as any delay may not be the sole responsibility of the credit union. Whether any "violation" was caused willfully or not should be a determining factor in any penalty assessment.**
21. Should part 715 require credit unions to notify NCUA in writing when they enter into an engagement with an auditor, and/or when an engagement ceases by reason of the auditor's dismissal or resignation? In cases of dismissal/resignation, should credit union be required to include reasons? **No. It is ACUIA's position that there would be no regulatory purpose for requiring this information outside of the normal NCUA examination process. Credit unions typically evaluate external audit services periodically and submit requests for proposal to other audit firms. Documentation of such a process is retained by the credit union. Such a requirement to notify NCUA would only create additional burden of paperwork on credit unions.**
22. Should supervisory committee members be prohibited by regulation from executing engagement letters that contain language limiting various forms of auditor liability to the credit union? Should supervisory committees be prohibited from waiving the auditor's punitive damages liability? **ACUIA believes that since the introduction of SOX, external audit firms have carefully needed to tailor their engagement letters so to more clearly define liability. The concern here is that would the elimination of liability clauses in the engagement letter result in higher audit expense to credit unions. As external audit firms mostly follow AICPA standards during such examinations, ACUIA would suggest that NCUA consider a review of those standards, professional standards, and guidance of the AICPA before making any determination in this regard. As for waiving the auditor's punitive damages liability, ACUIA strongly believes it should be prohibited.**

ACUIA appreciates this opportunity to provide response relative to possible modifications to NCUA's Supervisory Committee audit rules.

Sincerely,

ACUIA Board of Directors

ACUIA is an international professional organization dedicated to the practice of internal auditing in credit unions. Our objectives are:

- to unify and encourage cooperative relationships among credit union internal auditors to facilitate the exchange of information and ideas;***
- to promote professional standards for internal auditors in credit unions;***
- to provide educational opportunities for developing and enhancing audit and leadership skills;***
- to provide guidance for internal auditing of credit unions;***
- to assist in the development and retention of internal audit functions at credit unions and;***
- to communicate professional opportunities for internal auditors within the credit union industry.***